



Rating  
**Buy**

Asia  
China

Consumer  
Retail / Wholesale Trade

Company  
**Gree**

Reuters 000651.SZ    Bloomberg 000651 CH    Exchange SHZ    Ticker 000651

Date  
12 December 2017

## Company Update

Price at 11 Dec 2017 (CNY)	43.44
Price target - 12mth (CNY)	49.20
52-week range (CNY)	47.80 - 23.79
Shenzhen Index	2,008

## Comments from Chairman Dong

On 9 December 2017, Gree's chairman Mingzhu Dong was invited by the China Entrepreneur Summit to give a speech on several topics, including Gree's automation strategy and 2017 performance:

- The automation reform and diversification strategy are bearing fruits.** In her speech, Ms. Dong commented that Gree began to diversify its businesses in recent years. In addition air-conditioning business, it has entered into the field of small appliances, smart manufacturing, smart phones etc. Gree is undergoing automation reform. The company considered using the domestic equipment before, but it finally chose the imported German devices due to the higher precision. But as a long term plan, Gree decided to enter into the field of industrial manufacturing in 2013. Currently, Gree's CNC machine, and robots are not only provided for internal use, but also for other industries. Ms. Dong said that all of the devices in Zhuhai Silver Dargon (a company invested by Ms Dong privately) were produced by Gree.
- Preview of 2017 results.** According to Ms. Dong, Gree 's 2017-ytd revenue increased RMB 40bn (2016 revenue: RMB108.3bn) as compared with last year's same period, and its NP margin was 15%.

### Deutsche Bank view

With 2017 sales increased by RMB40bn, this implies 2017 total gross revenue will reach RMB148bn, which beat DB's forecast and market consensus by 5% and 4%, respectively. As for NP margin, her guidance is 0.3/0.8 ppt higher than DB's forecast (14.7%) and market consensus (14.2%), respectively. Management did not comment on Ms Dong's 2017 sales and NPM data.

**Better product mix: an important positive in 2018 restocking that is not fully priced in.** Gree's strong net margin could be driven by better product mix. In our recent channel checks we noticed that distributors (starting from the new air conditioner year) are focusing more on improving their product mix than in previous years, clearing inventory to recover cash. This may drive better profitability for air conditioner brands (on top of strong volume growth which is likely in the price). Profitability expansion should be universal, as Midea previously indicated that its core brand gross margin has improved by 2-3ppt YoY during

### Valuation & Risks

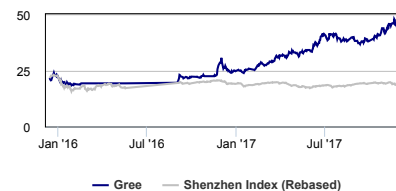
Anne Ling

Research Analyst  
+852-2203 6177

John Chou

Research Analyst  
+852-2203 6196

### Price/price relative



Performance (%)	1m	3m	12m
Absolute	-4.9	17.1	60.9
Shenzhen Index	-5.9	-3.6	-7.3

Source: Deutsche Bank

### Key indicators (FY1)

ROE (%)	36.2
Net debt/equity (%)	-179.1
Book value/share (CNY)	10.35
Price/book (x)	4.2
Net interest cover (x)	-
Operating profit margin (%)	16.4

Source: Deutsche Bank

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3Q17 analyst meeting. In our model, we expect GPM for 4Q17F to reach 32.3% for Gree vs 3Q17's 30.9% and 4Q16's 29.4%.

Figure 1: DB forecast vs. Market forecast

RMBm	DB forecast			Market forecast (Standard)			% change vs. market		
	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E	FY17E	FY18E	FY19E
Gross sales	142,451	158,411	175,222	142,184	157,735	176,489	0%	0%	-1%
EBIT	23,132	24,727	26,907	21,849	23,768	26,889	6%	4%	0%
EBIT margin	16.2%	15.6%	15.4%	15.4%	15.1%	15.2%	6%	4%	1%
Net profit	20,995	22,726	24,900	20,246	23,182	26,124	4%	-2%	-5%
NP margin	14.7%	14.3%	14.2%	14.2%	14.7%	14.8%	4%	-2%	-4%

Source: Deutsche Bank; Bloomberg Finance LP

Forecasts and ratios

Year End Dec 31	2015A	2016A	2017E	2018E	2019E
Sales (CNYm)	99,812.6	108,682.7	141,026.4	156,827.0	173,469.9
EBITDA (CNYm)	14,315.1	15,515.4	24,862.1	26,524.8	28,787.4
Reported NPAT (CNYm)	12,532.4	15,421.0	20,995.0	22,726.5	24,899.5
Reported EPS FD(CNY)	2.08	2.56	3.49	3.78	4.14
DB EPS FD(CNY)	2.08	2.56	3.49	3.78	4.14
DB EPS growth (%)	-11.5	23.0	36.1	8.2	9.6
PER (x)	10.3	8.3	12.4	11.5	10.5
EV/EBITDA (x)	2.7	2.3	5.7	4.6	3.5
DPS (net) (CNY)	1.50	1.50	2.09	2.27	2.48
Yield (net) (%)	7.0	7.1	4.8	5.2	5.7

Source: Deutsche Bank estimates, company data



Model updated: 13 November 2017

Running the numbers

Asia  
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Retail / Wholesale Trade

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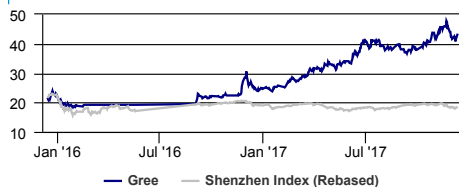
Buy

Price (11 Dec 17) CNY 43.44  
Target Price CNY 49.20  
52 Week range CNY 23.79 - 47.80  
Market cap (m) CNYm 261,323  
USDm 39,492

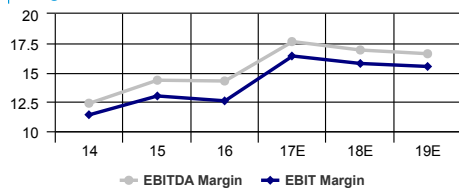
Company Profile

Gree is mainly engaged in the manufacture and distribution of household air conditioners and central air conditioners.

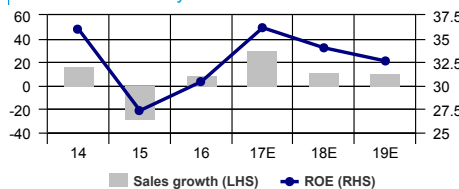
Price Performance



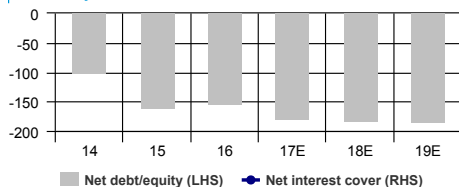
Margin Trends



Growth & Profitability



Solvency



Anne Ling

+852 2203 6177

anne.ling@db.com

Fiscal year end 31-Dec 2014 2015 2016 2017E 2018E 2019E

Financial Summary

DB EPS (CNY)	2.35	2.08	2.56	3.49	3.78	4.14
Reported EPS (CNY)	2.35	2.08	2.56	3.49	3.78	4.14
DPS (CNY)	1.50	1.50	1.50	2.09	2.27	2.48
BVPS (CNY)	14.7	7.9	9.0	10.3	11.9	13.5
Weighted average shares (m)	6,016	6,016	6,016	6,016	6,016	6,016
Average market cap (CNYm)	83,062	128,915	127,585	261,323	261,323	261,323
Enterprise value (CNYm)	28,595	38,315	36,239	140,692	122,075	102,167

Valuation Metrics

P/E (DB) (x)	5.9	10.3	8.3	12.4	11.5	10.5
P/E (Reported) (x)	5.9	10.3	8.3	12.4	11.5	10.5
P/BV (x)	1.20	2.83	2.75	4.20	3.66	3.21
FCF Yield (%)	20.2	34.2	11.6	16.1	12.4	13.4
Dividend Yield (%)	10.9	7.0	7.1	4.8	5.2	5.7
EV/Sales (x)	0.2	0.4	0.3	1.0	0.8	0.6
EV/EBITDA (x)	1.7	2.7	2.3	5.7	4.6	3.5
EV/EBIT (x)	1.8	3.0	2.6	6.1	4.9	3.8

Income Statement (CNYm)

Sales revenue	138,643	99,813	108,683	141,026	156,827	173,470
Gross profit	50,609	33,861	36,591	45,473	50,940	56,251
EBITDA	17,171	14,315	15,515	24,862	26,525	28,787
Depreciation	1,357	1,338	1,838	1,730	1,798	1,881
Amortisation	0	0	0	0	0	0
EBIT	15,814	12,977	13,678	23,132	24,727	26,907
Net interest income/(expense)	942	1,929	4,846	2,092	2,577	3,009
Associates/affiliates	-4	3	8	6	6	6
Exceptionals/extraordinary	0	0	0	0	0	0
Other pre-tax income/(expense)	0	0	0	0	0	0
Profit before tax	16,752	14,909	18,531	25,229	27,310	29,921
Income tax expense	2,499	2,286	3,007	4,093	4,431	4,855
Minorities	98	91	104	141	153	167
Other post-tax income/(expense)	0	0	0	0	0	0
Net profit	14,155	12,532	15,421	20,995	22,726	24,900
DB adjustments (including dilution)	0	0	0	0	0	0
DB Net profit	14,155	12,532	15,421	20,995	22,726	24,900

Cash Flow (CNYm)

Cash flow from operations	18,556	46,954	18,070	44,415	35,066	37,959
Net Capex	-1,777	-2,885	-3,277	-2,397	-2,666	-2,949
Free cash flow	16,779	44,070	14,793	42,017	32,400	35,010
Equity raised/(bought back)	0	0	0	0	0	0
Dividends paid	-4,676	-9,525	-9,180	-12,597	-13,636	-14,940
Net inc/(dec) in borrowings	2,417	1,526	792	0	0	11,363
Other investing/financing cash flows	1,483	-1,796	389	0	0	0
Net cash flow	16,004	34,274	6,793	29,420	18,764	31,433
Change in working capital	6,559	32,374	-85	20,587	10,057	10,593

Balance Sheet (CNYm)

Cash and other liquid assets	54,546	88,820	95,613	125,033	143,797	163,867
Tangible fixed assets	17,948	18,588	21,636	22,303	23,171	24,239
Goodwill/intangible assets	0	0	0	0	0	0
Associates/investments	9,946	13,397	8,155	8,161	8,167	8,173
Other assets	73,791	40,894	56,965	69,833	76,120	82,741
Total assets	156,231	161,698	182,370	225,331	251,255	279,021
Interest bearing debt	9,046	10,572	11,363	11,363	11,363	11,363
Other liabilities	102,054	102,560	116,083	150,505	167,186	184,824
Total liabilities	111,099	113,131	127,446	161,868	178,549	196,188
Shareholders' equity	44,153	47,521	53,864	62,262	71,353	81,312
Minorities	979	1,045	1,060	1,201	1,354	1,521
Total shareholders' equity	45,131	48,567	54,924	63,463	72,706	82,833
Net debt	-45,500	-78,248	-84,250	-113,670	-132,434	-152,504

Key Company Metrics

Sales growth (%)	16.4	-28.0	8.9	29.8	11.2	10.6
DB EPS growth (%)	30.2	-11.5	23.0	36.1	8.2	9.6
EBITDA Margin (%)	12.4	14.3	14.3	17.6	16.9	16.6
EBIT Margin (%)	11.4	13.0	12.6	16.4	15.8	15.5
Payout ratio (%)	63.7	72.0	58.5	60.0	60.0	60.0
ROE (%)	36.0	27.3	30.4	36.2	34.0	32.6
Capex/sales (%)	1.3	2.9	3.0	1.7	1.7	1.7
Capex/depreciation (x)	1.3	2.2	1.8	1.4	1.5	1.6
Net debt/equity (%)	-100.8	-161.1	-153.4	-179.1	-182.1	-184.1
Net interest cover (x)	nm	nm	nm	nm	nm	nm

Source: Company data, Deutsche Securities estimates



# Appendix 1

## Important Disclosures

\*Other information available upon request

Disclosure checklist			
Company	Ticker	Recent price*	Disclosure
Gree	000651.SZ	43.02 (CNY) 12 Dec 2017	14

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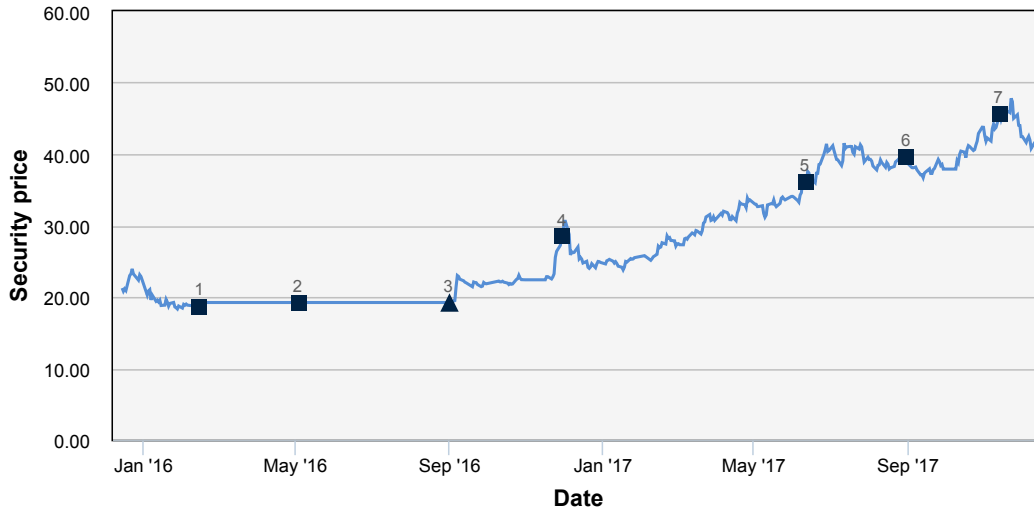
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Historical recommendations and target price. Gree (000651.SZ)

(as of 12/11/2017)



Current Recommendations

- Buy
- Hold
- Sell
- Not Rated
- Suspended Rating

\*\* Analyst is no longer at Deutsche Bank

1.	02/15/2016	Hold, Target Price Change CNY 16,29	Richard Rui-Huang**	5.	06/12/2017	Buy, Target Price Change CNY 38,87	Anne Ling
2.	05/04/2016	Hold, Target Price Change CNY 18,10	Richard Rui-Huang**	6.	08/31/2017	Buy, Target Price Change CNY 44,40	Anne Ling
3.	09/01/2016	Upgraded to Buy, Target Price Change CNY 24,91	Richard Rui-Huang**	7.	11/13/2017	Buy, Target Price Change CNY 49,20	John Chou
4.	11/30/2016	Buy, Target Price Change CNY 28,48	Richard Rui-Huang**				

Equity Rating Key

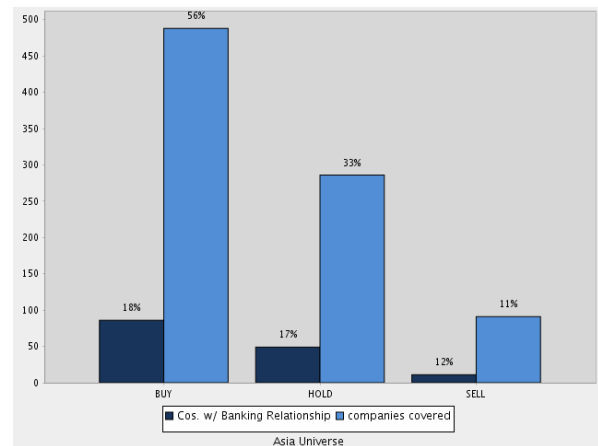
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Sell: Based on a current 12-month view of total share-holder return, we recommend that investors sell the stock.

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Equity rating dispersion and banking relationships





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## David Folkerts-Landau

Group Chief Economist and Global Head of Research

Raj Hindocha  
Global Chief Operating Officer  
Research

Michael Spencer  
Head of APAC Research  
Global Head of Economics

Steve Pollard  
Head of Americas Research  
Global Head of Equity Research

Anthony Klarman  
Global Head of  
Debt Research

Paul Reynolds  
Head of EMEA  
Equity Research

Dave Clark  
Head of APAC  
Equity Research

Pam Finelli  
Global Head of  
Equity Derivatives Research

Andreas Neubauer  
Head of Research - Germany

Spyros Mesomeris  
Global Head of Quantitative  
and QIS Research

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### International Production Locations

#### Deutsche Bank AG

Deutsche Bank Place  
Level 16  
Corner of Hunter & Phillip Streets  
Sydney, NSW 2000  
Australia  
Tel: (61) 2 8258 1234

#### Deutsche Bank AG

Mainzer Landstrasse 11-17  
60329 Frankfurt am Main  
Germany  
Tel: (49) 69 910 00

#### Deutsche Bank AG

Filiale Hongkong  
International Commerce Centre,  
1 Austin Road West, Kowloon,  
Hong Kong  
Tel: (852) 2203 8888

#### Deutsche Securities Inc.

2-11-1 Nagatacho  
Sanno Park Tower  
Chiyoda-ku, Tokyo 100-6171  
Japan  
Tel: (81) 3 5156 6770

#### Deutsche Bank AG London

1 Great Winchester Street  
London EC2N 2EQ  
United Kingdom  
Tel: (44) 20 7545 8000

#### Deutsche Bank Securities Inc.

60 Wall Street  
New York, NY 10005  
United States of America  
Tel: (1) 212 250 2500

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